



FILED

11-07-06

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking Concerning
Relationship Between California Energy Utilities
And Their Holding Companies And
Non-Regulated Affiliates.

Rulemaking 05-10-030
(Filed October 27, 2005)

**JOINT RULING OF ASSIGNED COMMISSIONER AND ADMINISTRATIVE LAW
JUDGE INVITING COMMENT ON FURTHER PROPOSAL FOR REVISIONS TO
RULES IV, V AND VI OF THE AFFILIATE TRANSACTION RULES APPLICABLE TO
LARGE CALIFORNIA ENERGY UTILITIES AND CORRECTING OMISSION IN
DRAFT REVISIONS TO GO-77 ATTACHED TO THE PROPOSED DECISION**

Summary

Respondents and other parties may file and serve Comments, due November 17, 2006, on a further proposal for modification of the Affiliate Transaction Rules applicable to large California energy utilities. The proposal has two parts.

The first requires key officers at each utility and holding company to annually certify their individual compliance with the Affiliate Transaction Rules. This certification requirement would be added to Rule VI (Regulatory Compliance) in lieu of the Proposed Decision's recommendation to modify Rule IV (Disclosure and Information) to require semi-annual reporting of six categories of informational exchanges between a utility and its holding company.

The second part concerns compliance with two subsections of Rule V (Separation) -- the subsections titled V E (Corporate Support) and V G (Employees) -- and provides a utility and its holding company with an election. Accordingly, Rule V would be modified to provide that if these corporate entities prefer to retain the provisions on shared services or shared

employees/consultants/contractors found in the existing Affiliate Transaction Rules, they must eliminate any duplication of personnel among key corporate officers. If they prefer not to eliminate overlap among key officers, then they must cease to share the following services: legal, regulatory affairs and lobbying.

The Ruling also includes a corrected copy of Appendix B of the Proposed Decision, consisting of draft General Order (GO) 77-M. Like the proposed revisions to the Affiliate Transaction Rules, the proposed revisions to GO 77 are intended to apply only to Respondents. Accordingly, draft GO 77-M has been corrected to clearly state that. The existing, unmodified reporting rules (those now in GO 77-L) continue to apply to all other utilities; hence the paragraph currently applicable to utilities having gross operating revenues of \$1 billion or more has been reinserted, together with the explanation that it is applicable to all such utilities other than Respondents.

Background

The Proposed Decision was mailed on October 10, 2006 for public review under Pub. Util. Code § 311(g)(1) and Rule 14.3 of the Commission's Rules of Practice and Procedure. On October 18, Respondents and other parties participated in Oral Argument. While the Proposed Decision was properly noticed for consideration on the agenda for the Commission's November 9 public meeting, it has been held to the November 30 meeting to provide additional time to consider the Comments and Reply Comments filed to date and to permit additional Comments, consistent with this Ruling.

Discussion

One of the concerns underlying this rulemaking is the potential for a utility's parent holding company to serve as a conduit, whether intentionally or inadvertently, for the kinds of information that the existing Affiliate Transaction

Rules prohibit the utility and its affiliate from sharing directly. The Proposed Decision attempts to address this concern by imposing reporting requirements and by limiting shared services, consultants and contractors.

At Oral Argument and in their Comments on the Proposed Decision, Respondents have asserted that the proposal to amend Rule IV (Disclosure and Information) to require semi-annual reporting of six categories of informational exchanges between a utility and its holding company would require burdensome note taking, interfere with legitimate, daily corporate communications and fail to prevent abuse. Likewise, they contend that imposing further limitations on shared services, etc., would render the holding company structure inefficient and ineffective.

For example, Respondents state: “Indeed, if the Commission does not trust executives to comply with the existing anti-conduit rules, then a rule that would impose a recording requirement would add nothing because there would be no basis for believing that the covered communications were properly recorded.” (Respondents Comments, p. 21.) One of Respondents’ spokesmen made the same point at Oral Argument, stating: “... the key people at the holding company that have the obligation to the board and to – under Sarbanes-Oxley, if they don’t intent to honor the anti-conduit rule, none of the rest of this burdensome activity works.” (Tr. 39:1-5.) One Commissioner present, who expressed a strong concern about the burden note taking would impose, nonetheless remarked: “One fellow I used to work for used to say, “Trust, but verify.” (*Id.* at 47:14-15.) The Commissioner also observed: “... somewhere along the line there needs to be some comfort in the public that we get what we need in the process. So the point is really balance...” (*Id.* at 47:27-48:2.) The

two-part proposal put forward by this Ruling seeks to explore another approach to finding such balance.

The first part of the proposal would require each key officer at a utility and its holding company parent to annually certify under penalty of perjury to individual compliance with the Affiliate Transaction Rules, including all existing anti-conduit provisions, as a part of Rule VI (Regulatory Compliance). In return, the Proposed Decision's recommendation to require semi-annual reporting of six categories of informational exchanges between a utility and its holding company under Rule IV (Disclosure and Information) would be deleted. Specifically, this proposal consists of deleting the Proposed Decision's Rule IV C (Information a Utility Must Provide to the Commission) and adding a new Rule VI E (Officer Certification). For the purposes of this proposal, key officers include the Chair of the entire corporate enterprise, the President or other functional equivalent at the utility and its holding company parent, the chief executive officer at each, the chief financial officer at each, and the chief regulatory officer or other functional equivalent at each.

The second part of the proposal concerns compliance with Rules V E (Corporate Support) and V G (Employees), which are both part of Rule V (Separation). As currently effective, Rule V E permits a utility and its holding company parent to share "corporate oversight, governance, support systems and personnel" and provides examples of services that may be shared and those that may not be shared. Existing Rule V G bans joint employees, except in areas of permitted shared services. The Proposed Decision recommends revisions to the lists of permitted and prohibited shared services and in particular, would prohibit sharing of regulatory affairs, lobbying, risk management and all legal services except those necessary to the provision of authorized shared services.

The Proposed Decision also recommends revisions to Rule V G to prohibit the sharing of consultants and contractors other than independent auditors.

This Ruling asks for comment on a different approach, one that provides a utility and its holding company with an election. If these corporate entities prefer to retain the status quo in the Affiliate Transaction Rules on the sharing of services, employees, consultants and contractors, then they must eliminate any duplication of personnel among key corporate officers. If they prefer not to eliminate overlap among key officers, then they must cease to share the following services: legal, regulatory affairs and lobbying. For the purposes of this proposal, the key officers are the same ones identified above. A reasonable implementation timeline would need to be set, perhaps 180 days from the effective date of the Commission decision modifying the Affiliate Transaction Rules to permit the election. Rules V E and V G would be revised to provide for the election. Having elected one course of compliance, the utility and its holding company parent would not be permitted to change course in the future except upon Commission review and approval of an advice letter filing.

This Ruling also includes a corrected copy of Appendix B of the Proposed Decision, consisting of draft General Order (GO) 77-M. We intend the correction to make no substantive change (1) in existing law, as applicable to utilities other than Respondents or (2) in the proposed modifications to existing law, applicable only to Respondents, which have been discussed to date in this rulemaking. Parties may comment on the corrections, if they see a need to do so.

We note, however, that we are unaware of any opposition to draft GO 77-M. Respondents' Comments seek one minor modification (a two month delay in

the reporting deadline from March 31 to May 31¹), but otherwise unequivocally state: “Respondents support the proposed changes to General Order 77-L as codified in new General Order 77-M.” (Respondents October 30, 2006 Comments, p. 29.)

The corrections consist in reinserting in draft GO 77-M an existing paragraph that was unintentionally dropped from the working draft. That paragraph makes the existing general order applicable to utilities having gross operating revenues of \$1 billion or more. It will continue to apply to all such utilities other than Respondents, consistent with Pub. Util. Code § 1708, which requires notice and opportunity to be heard before the Commission may alter a prior decision. This rulemaking applies only to Respondents any modifications to existing law adopted by the Commission will apply only to Respondents.

¹ Respondents explain they need the additional time to obtain an independent auditor’s letter because of tax season workload. We anticipate the Commission will be persuaded to make this minor modification.

Therefore, **IT IS RULED** that any party may file and serve comments by November 17, 2006 on:

- (a) the two-part proposal discussed in the body of this Ruling and appended hereto as Appendix A; and
- (b) the corrected copy of draft GO 77-M discussed in the body of this Ruling and appended hereto as Appendix B.

Dated November 7, 2006, at San Francisco, California.

/s/ GEOFFREY F. BROWN

Geoffrey F. Brown
Assigned Commissioner

/s/ JEAN VIETH

Jean Vieth
Administrative Law Judge

INFORMATION REGARDING SERVICE

I have provided notification of filing to the electronic mail addresses on the attached service list.

Upon confirmation of this document's acceptance for filing, I will cause a copy of the filed document to be served upon the service list to this proceeding by U.S. mail. The service list I will use to serve the copy of the filed document is current as of today's date.

Dated November 7, 2006, at San Francisco, California.

/s/ JOYCE TOM

Joyce Tom

N O T I C E

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